

STATE OF MAINE  
PUBLIC UTILITIES COMMISSION

April 22, 2004

ORDER APPROVING  
STIPULATION

BANGOR HYDRO-ELECTRIC COMPANY  
Request for an Accounting Order (PERC  
Settlement Agreement

Docket No. 2004-5

MAINE PUBLIC UTILITIES COMMISSION  
Investigation Into BHE's Stranded Cost  
Revenue Requirements and Rates

Docket No. 2004-112

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WELCH, Chairman; DIAMOND and REISHUS, Commissioners

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**I. SUMMARY**

We approve a Stipulation and find that Bangor Hydro-Electric Company (BHE or Company) acted reasonably to mitigate its stranded costs by entering into a Settlement Agreement with the Penobscot Energy Recovery Company (PERC). The Settlement Agreement resolves a dispute concerning the rates paid by BHE to PERC under a Power Purchase Agreement between BHE and PERC. We also direct BHE to account for the financial transactions associated with the Settlement Agreement as provided for in the Stipulation. Finally, we stay the proceeding in Docket No. 2004-112, our current investigation of BHE's stranded cost rates, until we either resume processing the case to establish new stranded cost rates by March 1, 2005, the end of the current stranded cost rate-setting period or until any party requests a change in stranded costs rates due to a change in BHE's financial condition.

**II. BACKGROUND**

BHE and PERC entered into the Power Purchase Agreement (PPA) on June 21, 1984. Under the PPA, BHE is obligated to purchase all of the electric energy and capacity produced at a Qualifying Facility (a municipal waste-to-energy plant) owned by PERC. PERC began making deliveries to BHE under the PPA in February 1988.

Under Article III of the PPA, the purchase price contains a component, known as the Variable Component, that is subject to an inflation adjustment on April 1 of each year during the term of the PPA. During each year after 1988 until 2002, BHE adjusted the Variable Component on January 1 instead of April 1, mistakenly believing that the PPA required the adjustment on January 1. As a result of this mistake, BHE calculated that it overpaid PERC by \$1,287,127.37 for power delivered under the PPA through December 31, 2002.

BHE became aware of its mistake in early 2003. Beginning in that year, BHE calculated the PERC rate by adjusting for the Variable Component on April 1 rather than January 1. Also in 2003, BHE sought to recover the overpayment of \$1,287,127.37, that had occurred from 1989 through 2002.

PERC denied any liability for the mistaken overpayment that occurred prior to 2003. However, PERC claimed that BHE had actually underpaid PERC by approximately \$10 million because BHE had begun to escalate the Variable Component in 1989, the year following the initial delivery rather than 1985, the year following the execution of the PPA. BHE disagreed with PERC's suggested contract interpretation and denied any liability to PERC.<sup>1</sup>

BHE and PERC reached a settlement of these claims related to calculation of the Variable Component. By the terms of the Settlement Agreement, PERC will reimburse BHE \$475,000, in equal monthly payments over two years, in full satisfaction of BHE's claim against PERC for reimbursement of the overpayment by BHE. PERC also releases BHE from any liability it may have to PERC as a result of BHE's failure to begin escalation of the Variable Component in 1985. The Settlement Agreement is conditioned upon a finding by the Commission that the Settlement Agreement reflects a reasonable effort by BHE to mitigate stranded costs.

On January 8, 2004, BHE filed a Petition to Reopen and Petition for Accounting Order with the Commission. BHE asked that the Commission find that the Settlement Agreement reflects a reasonable effort by BHE to mitigate stranded costs. BHE asserted that the Settlement Agreement is in the best interests of BHE's customers and should directly benefit its customers. To ensure that customers receive the benefits, BHE requested an accounting order from the Commission authorizing BHE to defer the net revenue it will receive under the Settlement Agreement. By net revenue, BHE meant that its litigation expenses and the reduction in BHE's profit sharing payments from PERC<sup>2</sup> should be offset against the revenue received pursuant to the Settlement Agreement.

BHE filed its Petition in Docket No. 2001-239, the most recent investigation into the Company's stranded costs. The Commission concurred that BHE's Petition should be treated as a reopening of Docket No. 2001-239. For administrative convenience, however, the re-opened Docket No. 2001-239 was assigned a new docket number, and all filings related to BHE's petition have been and will be placed in the file labeled "Docket No. 2004-5."

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<sup>1</sup> BHE estimated that PERC's contract interpretation would cost an additional \$30 million over the term of the PPA.

<sup>2</sup> As a result of a 1998 amendment to the PPA, entered into in conjunction with Finance Authority of Maine (FAME) refinancing of PERC's debt instruments, BHE now receives a portion of the profits earned by PERC. Accordingly, if PERC's sales revenue decreases, its profits decrease, as does BHE's share.

On February 10, 2004, BHE filed a request that the Commission investigate the Company's current stranded cost rates. In its request, BHE noted that it forecasted a significant stranded cost earnings deficiency over the next twelve months. BHE suggested an informal discovery and negotiation process in hopes that its rates could be adjusted within a few weeks rather than months.

The Commission initiated a formal investigation on February 12, 2004 to determine whether BHE's current stranded costs are substantially inaccurate, in accordance with 35-A M.R.S.A. § 3208. The new stranded costs investigation was assigned Docket No. 2004-112. The Office of the Public Advocate (OPA) and the Industrial Energy Consumer Group (IECG) were granted intervenor status. Central Maine Power Company (CMP) was granted intervention for the limited purpose of receiving filings and filing briefs on legal or policy issues.

Discovery, including technical conferences, was conducted throughout February and March, in both Docket Nos. 2004-5 and 2004-112. The Advisory Staff also convened several settlement conferences during March. As a result of discussions at the settlement conferences, a Stipulation was filed with the Commission on April 8, 2004. BHE, OPA and the IECG join the Stipulation. The Advisory Staff recommends that the Commission approve the Stipulation.

### **III. DESCRIPTION OF THE STIPULATION**

The Stipulating Parties recommend that the Commission find that the Settlement Agreement between BHE and PERC constitutes a reasonable effort by BHE to mitigate its stranded costs. They also agree that the monthly payments that will be made by PERC to BHE under the terms of the Settlement Agreement should be deferred on BHE's books of account and be returned to ratepayers in a future stranded cost rate case. The Stipulating Parties, however, adjust the monthly payments to reflect the approximate reductions to the profit-sharing payments that BHE will receive because of the Settlement Agreement payments made to BHE. Thus, the Stipulation calls for deferral of two-thirds of the monthly payments.

The Stipulation also requires BHE to defer the difference in the PERC PPA prices that were assumed in setting rates when it was assumed the Variable Component was adjusted on Jan. 1, in Docket No. 2001-239, and the PERC prices as corrected and actually paid to PERC in 2003 and 2004 (and that will be paid in 2005), when the Variable Component was adjusted on April 1 rather than January 1. This cost deferral is reduced by one-sixth, to account for 50% of the profit sharing that BHE loses due to the lower PERC profits.

BHE agrees that it will not defer, and will not seek recovery in rates, any of the legal expenses that the Company incurred in its dispute with PERC about the calculation of the Variable Component, including its costs associated with Docket No. 2004-5.

Lastly, the Stipulating Parties agree to defer further processing of Docket No. 2004-112 until such time as is necessary to establish new stranded costs rates for effect on March 1, 2005. In other words, BHE is no longer seeking a stranded costs rate adjustment based upon its February forecast.

#### IV. DECISION

As we have now stated on numerous occasions, to approve a stipulation the Commission must find that:

1. the parties joining the stipulation represent a sufficiently broad spectrum of interests that the Commission can be sure that there is no appearance or reality of disenfranchisement;
1. the process that led to the stipulation was fair to all parties; and
2. the stipulated result is reasonable and not contrary to legislative mandate.

See *Central Maine Power Company, Proposed Increase in Rates*, Docket No. 92-345(II), Detailed Opinion and Subsidiary Findings (Jan. 10, 1995), and *Maine Public Service Company, Proposed Increase in Rates (Rate Design)*, Docket No. 95-052, Order (June 26, 1996).

We have also recognized that we have an obligation to ensure that the overall stipulated result is in the public interest. See *Northern Utilities, inc., Proposed Environmental Response Cost Recovery*, Docket No. 96-678, Order Approving Stipulation (April 28, 1997). We find that the proposed Stipulation in this case meets all the above criteria.

The Stipulation before us was entered into between the Company, the OPA and the IECG. In past cases, we have found that the utility and the OPA, often representing opposite views in the ratemaking process, constitute a sufficiently broad spectrum of interests to satisfy the first criterion. See *Public Utilities Commission, Investigation of Stranded Cost Recovery, Transmission and Distribution Utility Revenue Requirements and Rate Design of Bangor Hydro-Electric Company (Phase II)*, Docket No. 99-185, Order Approving Stipulation (Maine Public Service Company) at 3 (Aug. 11, 2000). The IECG, representing large consumers, makes the spectrum of interests that are represented by the Stipulation even broader.

Based on the record before us, we believe that the process that led to this Stipulation was fair and open. Indeed the process was initiated at a publicity-announced settlement conference conducted by our Staff, with all parties invited to participate. Furthermore, the Advisors participated in the entire negotiating process. We therefore find that the second criterion for approval has also been satisfied.

Finally, we conclude that the result of the Stipulation is reasonable, not contrary to legislative mandates, and consistent with the public interest. The Stipulation resolves all issues raised by BHE's Petition in Docket No. 2004-5. The Advisory Staff explained their reasoning for helping to negotiate and for supporting the Stipulation.<sup>3</sup> The Advisors believed that BHE's petition raised two distinct issues. First, whether the PERC-BHE Settlement Agreement was a reasonable resolution of the dispute between BHE and PERC to recover the overpayment by BHE when it miscalculated the Variable Component. In addition, the Staff questioned whether BHE's actions were prudent when it miscalculated the Variable Component, such that BHE paid too much for power since the second year of PERC's operation.

Through discovery responses and technical conferences, the Advisors concluded that the Settlement Agreement was a reasonable resolution of the dispute over whether PERC should reimburse BHE for Variable Component overpayments. While the Advisors concluded that a court would likely determine that BHE had miscalculated the Variable Component, and therefore overpaid for power since 1989, it was far from clear that BHE would be able to recover for overpayments for the entire term. Equitable concepts such as *laches*, and the general six-year statute of limitation, presented valid defenses that reduced the chance for full recovery by BHE. Given the risks and costs of litigation, the Advisors reasoned that a payment of \$475,800 to BHE was reasonable.

Upon review of the PPA, the Advisors believed that it was likely that the Commission would find that BHE bore some culpability for the miscalculation of the Variable Component. Based upon that belief, the Advisor's suggested that a Stipulation should provide for BHE's shareholders to share in the cost of the miscalculated Variable Component. The Stipulation does so by denying BHE recovery of its legal expenses and by allowing ratepayers to "recover" the value of reduced PERC payments made by BHE beginning in 2003, since current rates reflect the erroneous, miscalculated PERC costs. In addition, BHE agreed to forego the opportunity to pursue a stranded cost rate change for effect before March 2005, at least based upon information available as of February, 2004.

We agree that the Stipulation presents a reasonable resolution of the issues raised by the PERC Settlement Agreement and BHE's petition to reset stranded cost rates, Docket No. 2004-112. Ratepayers should receive the benefit of payments to be made by PERC to BHE. We also agree that it is fair that BHE's shareholders contribute, although modestly, to costs caused by the miscalculation. In the context of BHE acting to correct its earlier mistake, we can approve a Stipulation that imposes a rather modest penalty.

Accordingly we,

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<sup>3</sup> The Stipulating Parties waived their right to require the Advisors to make any recommendation in writing with the opportunity for exceptions. Therefore the Advisors were free to discuss their recommendation with the Commissioners.

O R D E R

1. That the attached Stipulation is approved;
2. That the Settlement Agreement described above constitutes a reasonable effort by BHE to mitigate its stranded costs; and,
3. That BHE shall defer on its books of account the regulatory liabilities described in the Stipulation.

Dated at Augusta, Maine, this 22<sup>nd</sup> day of April, 2004.

BY ORDER OF THE COMMISSION

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Dennis L. Keschl  
Administrative Director

COMMISSIONERS VOTING FOR:      Welch  
   Diamond  
   Reishus

## NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.
2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within **21 days** of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320(1)-(4) and the Maine Rules of Appellate Procedure.
3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320(5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.